

Message Text

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ACTION EB-11

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INFO AMEMBASSY BEIRUT UNN

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SUBJECT: IMPROVED PETROLEUM PROSPECTS WILL EASE REVENUE SQUEEZE

SUMMARY. IT WILL SOON BECOME PUBLICLY KNOWN HERE THE EXTENT TO WHICH THE FISCAL POSITION OF THE VENEZUELAN GOVERNMENT IS IMPROVING AS A RESULT OF RAPIDLY- INCREASING PETROLEUM REVENUE. UNFORTUNATELY, THIS KNOWLEDGE IS LIKELY TO LESSEN THE INCENTIVE FOR VENEZUELAN GOVERNMENT TO TAKE TIMELY ACTION

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TO DEVELOP NEW PETROLEUM RESERVES THAT WILL BE NEEDED AS PRODUCTION POTENTIAL FROM EXISTING CONCESSION AREAS CONTINUES TO DECLINE. END SUMMARY.

1. THE EMBASSY'S AIRGRAM A-277, PETROLEUM INDUSTRY OUTLOOK REPORT, POINTS OUT THAT VENEZUELA IS " APPROACHING A CROSSROADS IN PETROLEUM POLICY IN WHICH BASIC DECISIONS WILL HAVE TO BE TAKEN AS TO HOW BEST TO DEAL WITH A SITUATION IN WHICH ITS MAIN SOURCE OF REVENUE AND NATIONAL WEALTH, OIL PRODUCTION, IS SHRINKING." THE AIRGRAM CONCLUDES THAT BEST MEANS OPEN TO VENEZUELA TO DEAL WITH THIS PROBLEM WOULD BE " TO UNDERTAKE A MAJOR PROGRAM TO DEVELOP PETROLEUM PRODUCTION IN NEW AREAS OUTSIDE OF EXISTING CONCESSIONS, SUCH AS ORINOCO PETROLEUM BELT."

2. WHAT THE EMBASSY DID NOT WISH TO SAY IN THAT UNCLASSIFIED MESSAGE IS THAT VENEZUELA IS NOW APPROACHING THAT " CROSSROADS" MUCH LESS SLOWLY THAN WOULD BE DESIRABLE IN TERMS OF INCENTIVE TO OPEN UP NEW PROSPECTIVE PETROLEUM AREAS TO FOREIGN INVESTMENT. GREATER THAN EXPECTED WORLD OIL PRICE INCREASES OVER PAST YEAR, AS A RESULT OF THE PARTICIPATION AGREEMENTS AND COMPENSATION FOR DEVALUATION OF US DOLLAR HAVE GREATLY EASED FISCAL SQUEEZE IN VENEZUELA AND HAVE POSTPONED FOR AT LEAST ONE TO TWO YEARS TIME WHEN THE DOWNWARD TREND OF PRODUCTION POTENTIAL IN CURRENT PETROLEUM CONCESSION AREAS WILL EXERCISE A STRONG ENOUGH DOWNWARD PRESSURE ON REVENUE TO FORCE GOVERNMENT TO MAKE A MAJOR EFFORT, WITH NECESSARY ASSISTANCE OF PRIVATE ENTERPRISE, TO DEVELOP NEW PETROLEUM PRODUCING AREAS.

3. WITH INCREASE IN TAX REFERENCE VALUES THAT TOOK PLACE ON JANUARY 1 (11-12 CENTS PER BARREL AVERAGE) AND ON MARCH 13 (27 CENTS PER BARREL AVERAGE) PLUS HIGHER FREIGHT PREMIUMS, AND WITH LIKELIHOOD THAT TOTAL OIL PRODUCTION WILL INCREASE 100-150 THOUSAND B/D THIS YEAR UNDER PRESSURE FROM A STRONG MARKET DEMAND AND FROM VENEZUELAN PENALTIES FOR UNDER PRODUCTION, VENEZUELAN GOVERNMENT IS LIKELY TO GET AS MUCH AS 1 BILLION BOLIVARES (\$233 MILLION MORE REVENUE THIS YEAR THAN IT ESTIMATED IN BUDGET.

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4. MOREOVER, IT IS LIKELY THAT OIL COMPANIES WILL BE ABLE TO MAINTAIN TOTAL OIL PRODUCTION ON A KIND OF PLATEAU FOR ANOTHER YEAR OR TWO BEFORE THE INEVITABLE DOWNWARD TREND OF PRODUCTION POTENTIAL ASSERTS ITSELF, BECAUSE POTENTIAL, EVEN THOUGH IT IS FALLING, IS STILL (AT 3.5 MILLION B/D) ABOVE PRODUCTION. CONSEQUENTLY, WITH ONLY MODEST PRICE INCREASES VENEZUELAN GOVERNMENT

SHOULD BE ABLE TO OBTAIN SUFFICIENT REVENUE TO MEET
ITS EXPENDITURE NEEDS FOR AT LEAST A COUPLE OF YEARS.

5. IT IS WORTH REVIEWING BRIEFLY WHAT CAUSED THIS GREAT
CHANGE IN VENEZUELA REVENUE SITUATION SINCE LAST YEAR
WHEN A FISCAL SQUEEZE WAS ON, AND IT APPEARED THAT EVEN
AFTER USING ALL STRATAGEMS - SUCH AS ONE TIME ACCELERA-
TIONS OF TAX PAYMENTS - VENEZUELA WOULD FACE AN UNAVOID-
ABLE REVENUE GAP BY 1974. BASICALLY, EXTERNAL FACTORS
WERE RESPONSIBLE. THE PRICE OF OIL IN PERSIAN GULF
TURNED OUT NOT TO BE SO FIRMLY FIXED BY TEHRAN AGREE-
MENTS AS IT HAD APPEARED. IN EARLY 1972, VENEZUELAN
OIL WAS ALREADY marginally UNCOMPETITIVE WITH EASTERN
HEMISPHERE OIL ON THE US EAST COAST, SO THAT VENEZUELA
COULD NOT THINK OF INCREASING ITS OIL PRICES IN SUBSE-
QUENT YEARS THROUGH 1975 ANY FASTER THAN PRICES WENT
UP IN PERSIAN GULF, AND PG PRICES WERE SUPPOSEDLY NOT
TO RISE MORE THAN SMALL PERCENTAGE ALLOWED SUCH YEAR
UNDER AUTOMATIC FORMULA IN AGREEMENTS. BUT, ARABS
THOUGHT UP, AND GOT COMPANIES TO ACCEPT, IDEA OF
"PARTICIPATION" WHICH ADDED TO COST OF OIL COMPANIES'
SHARE OF PG OIL. THEN, ANOTHER DEVALUATION OF DOLLAR
CVAPO PAYMENT OF COMPENSATION, WHICH AMOUNTED TO
ANOTHER PRICE INCREASE. MEANWHILE, OIL MARKETS
STRENGTHENED, AND TANKER RATES ROSE STRONGLY, WHICH
SO INCREASED COMPETITIVE POSITION OF VENEZUELAN OIL
IN "SHORT HAUL" US MARKET THAT SCOPE FOR AN EVEN
GREATER INCREASE IN TAX TAKE WAS OPENED UP, AN
OPPORTUNITY THAT VENEZUELA PROFITED FROM THROUGH ITS
"FREIGHT PREMIUM" FORMULA. THUS, WAS VENEZUELA ABLE TO
POSTPONE THE "INEVITABLE" FOR ANOTHER COUPLE OF YEARS.

6. CLEARLY, VENEZUELA SHOULD USE TO GOOD ADVANTAGE
BREATHING SPACE PROVIDED BY IMPROVED REVENUE PROS-
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PECTS, SINCE GETTING NEW OIL AREAS INTO PRODUCTION
WILL REQUIRE SUBSTANTIAL LEAD TIME. WHETHER VENE-
ZUELAN POLITICIANS WILL DO SO BEFORE THE PRESSURE OF
BUDGET DEFICITS IS ACTUALLY UPON THEM REMAINS TO BE
SEEN, AND IS TO BE DOUBTED.
MCCLINTOCK

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